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ANALYTICAL TOOLS FOR USAID ANTICORRUPTION PROGRAMMING IN THE EUROPE & EURASIA REGION

AUGUST 2005

This publication was produced for review by the United States Agency for International Development. It was prepared by the IRIS Center, at the University of Maryland.

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CONTRACT NUMBER

PCE-I-00-97-00042-00, Task Order 8

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INTRODUCTION

USAID and other donor agencies are increasingly aware of the need for effective strategies and tools for addressing corruption in the transition countries. Corruption represents the continued mingling of state and private interests, and decision-making through non-transparent channels of personal influence, which were both prevalent under the Communist system. It is reversing some of the gains achieved by the region since 1989, and continues to pose several threats. It can hold back economic reform by distorting government policies and by diverting private sector effort from value-added investment to lobbying and rent-seeking; and it tends to drive new firms underground, siphon resources offshore, and dampen incentives for foreign investment. When corruption seriously compromises the legal system—impacting the enforcement of contracts and property rights, and possibly the protection of public order and civil liberties—predation can reach catastrophic dimensions.

In light of the threats posed by corruption in the transition region, USAID has set out to refine its strategies and tools in this field. This paper builds on both the agency-wide strategy and the framework developed by the Europe and Eurasia (E&E) Bureau. The USAID Anti-Corruption Strategy (USAID 2005) stresses the need to confront both grand and administrative corruption, to use agency resources strategically, and to incorporate anti-corruption goals across different sectors of programming. The E&E Bureau framework addresses corruption in terms of five factors that contribute to corruption-resistance: Transparency, Accountability, Prevention, Enforcement, and Education (TAPEE). These factors can be employed to identify corruption-related strengths and weaknesses of state institutions, and to design USAID activities accordingly. However, the TAPEE framework needs to be supplemented by a broader consideration of driving forces in the political economy and social system of the country in question. Adopting this wider angle of vision, this paper lays out the *strategic issues* that USAID should take into account in deciding on anti-corruption elements in its programming.

Part 2 lays out key concepts and diagnostic approaches, emphasizing corruption issues in the transition countries. The presentation is based on a multidisciplinary analysis (mainly using methodologies from the New Institutional Economics and Political Science). On the basis of an adequate understanding of these fundamental issues, we present (in Part 3) a framework for anti-corruption strategies relevant to USAID's programs in the region. This framework will join a brief analysis of how corruption has been restrained in the past, together with a discussion of USAID's role in anti-corruption activities. We also identify and analyze program-relevant variables in USAID project environments in the region. In Part 4, we suggest the outlines of a strategy-development process, and we construct a set of illustrative transition-country scenarios based on those variables, drawing out some of the implications for USAID programs. The analysis generates a framework for developing and tailoring anti-corruption strategies and programming in the region. Part 5 concludes. The Annexes include more detailed exposition for those interested.

CORRUPTION: CONCEPTUAL BASICS

Anti-corruption strategies can add value only to the extent that they are based on a realistic understanding of corruption phenomena: their causes, consequences, and dynamics. This section presents a few key concepts in this area and suggests how they fit into a framework for understanding and addressing corruption – particularly in transition settings.

DEFINING CORRUPTION

A commonly used definition of corruption is,

“The abuse of public power (or public office) for private gain.”¹

We should unpack this definition a little:

- The “abuse” could be understood to include some or all of the following: a crime, an administrative violation, the infringement of a political standard, an ethical lapse.
- “Public power” could be defined as the authority of *any arm of the state*, including executive bodies, the legislature, and the judiciary, as exercised by *any agent* of these branches. More expansively, one might include any organization or activity that is funded or supervised by the state (e.g. a public foundation or a bank), and, even more sweepingly, *any* structure in which decision-making power over policies and resources is exercised by some representative, delegate, or fiduciary (e.g., a corporation or labor union).
- Lastly, “private gain” simply refers to personal, kin, partisan, or other narrow interests that benefit, instead of the relevant “public” or even at its expense.

CAUSES: INDIVIDUALIST AND STRUCTURAL DIMENSIONS

Corruption has several dimensions, and the standard diagnoses tend to diverge based on which dimension is given priority. Models that focus on individual behavior include, notably, the *principal-agent* paradigm. Models that focus on structural factors include what we term the *parallel systems* paradigm.

THE PRINCIPAL-AGENT PARADIGM

Corruption is often conceptualized as a *principal-agent* problem.² Line employees act on behalf of superiors, firm managers on behalf of owners, bureaucrats on behalf of elected officials and, ultimately, on behalf of the electorate. Principals need to select, monitor, and motivate their agents to act in accord with the former’s interests in producing, say, company profit or effective public policies and services. The agents, as implementers, are closer to the realities on the ground

¹ Klitgaard (1988), see also Transparency International (1996).

² Rose-Ackerman (1978), Klitgaard (1988), Bardhan (1997).

and therefore have access to information and opportunities that can benefit them – instead of (or at the expense of) their principals. Corruption happens when *the agent acts for her own gain in ways that are inconsistent with the interests of the principal*.

This simple relationship is described and addressed differently in different societies, each of which draws a boundary around those principal-agent problems that concern them most. Large areas of advantage-taking behavior may be considered innocent, while others – embezzlement, bribery, and cronyism, for example – are considered corrupt and are outlawed in whole or in part. Principal-agent analysis highlights the individual incentives at play here. These incentives reflect the flow of information, the range of the agent’s untrammelled power and discretion, and the tools available for principals to impose accountability on the agent.

While the principal-agent paradigm is a powerful tool for understanding corruption and for organizing efforts to combat it, nevertheless its focus on individual incentives limits its utility for the analysis of corruption. Moreover, its genesis in the theory of the firm brings with it the assumption of simplified preferences (e.g. maximizing profits). The sole owner of a business surely is motivated to earn profits, and will select, monitor, and motivate managers and employees accordingly. As the picture becomes more complex – in a large corporation or in the broader polity – conflicts emerge. Multiple shareholders have only fractional interests in share value and dividends, and so may not be motivated to supervise managers. Elected officials have multiple interests, as policymakers, politicians, businessmen, family heads, individuals – and these interests can come into conflict. Citizens are extremely diffuse, and diverse, as principals. They usually have little material reason to inform themselves in detail about the workings of government, and this gives officials and narrow interests at times wide scope to ignore or disserve public interests. The putative principals here have no real control over the agents’ incentives – and yet, even given all these deficiencies of agency, many countries successfully avoid (or reverse) serious corruption.

THE PARALLEL SYSTEMS PARADIGM

Alternatively, corruption has been conceptualized as a core feature of an informal *parallel system* of organization and allegiance that has only a tangential relationship with the formal state structure. If we were to set aside for a moment the formal roles of voter-official-bureaucrat and look at the social, economic, and political relationships among these actors, we may see a very different picture. For example, elected officials may owe allegiance to quite narrow business or ethnic interests, and distribute benefits accordingly.

One can imagine two charts, each depicting the governance of a given country, superimposed one over the other. “Chart One” would depict the formal structure of government, with hierarchical command relationships running, say, from the chief of state to ministers and bureaucrats; horizontal checks and balances might include the legislature and judiciary, and the electorate (within a structure provided by the constitution) as principal and source of authority. This is the chart that most anti-corruption frameworks are concerned with.

Our imaginary “Chart Two” would depict the main social, political, and economic links among the same country’s governing elite, including the main resource-flows. These links might be based on loyalty to groups from a shared region, military unit, social class, or ethnicity. Many of the same people sitting in official positions in the first chart also appear in this second chart, but “Chart Two” shows actual exchanges and alliances. It is these interactions, and the desire to keep them secret (especially where these are considered corrupt and/or illegal), that explains the widely observed “lack of political will for reform.” Thus, two officials who relate formally as principal (e.g. high-ranking supervisor) and agent (e.g. line bureaucrat) may also hold positions in a

network of kinship or patronage that is more important to them, in practical terms, and that implies certain exchanges (e.g. personal and family preferment in return for bribe shares and delivery of voting blocs). In short, formal principal-agent roles may not apply – or at least not in the same way – when we take overriding social factors into account.³

AN EXCHANGE PERSPECTIVE

As the above discussion illustrates, networks and alliances rely on *exchanges* to meet their objectives – and they may use elements of the state and the political system to mediate these exchanges. Many, perhaps most, such exchanges are corrupt. As Scott (1969, 1972) has suggested, political and administrative systems offer diverse mechanisms for exchange. In some systems (many of them longstanding democracies), electoral politics and policymaking provide the primary means of exchange, e.g. through campaign contributions or bribes influencing policy decisions. In other systems, interest articulation through the political system is either impossible (authoritarian regimes) or not highly developed (quasi- or new democracies). Here, exchange tends to occur by means of bribery in return for favorable administrative decisions, diversion of state resources, favoritism in hiring and tender awards, and the like. More recent studies of the transition countries (World Bank 2000) label these forms of influence “state capture” and “administrative corruption” respectively.

If state institutions can be used as instruments to carry out corrupt exchanges, then these institutions can also be suborned or weakened in order to facilitate, hide, or protect such transactions. A recent analysis underlines this point:

The causes and consequences of and solutions for corruption tend to be intertwined. Consider, for example, the relationship between corruption and the effectiveness of a country’s legal system. The level of corruption...may begin to rise in response to, say, an external shock. The political elite may find the increased income from corruption irresistible. Once corrupted, the elite will attempt to reduce the effectiveness of the legal and judicial systems through manipulation of resource allocation and appointments to key positions. Reduced resources will make it difficult for the legal system to combat corruption, thus allowing corruption to spread even more. Therefore, a weak judicial system becomes a cause as well as a consequence of corruption.⁴

A further implication of the above analysis is that *any* person, system, or institution can become involved in corrupt exchanges. This includes not only the usual suspects, such as low-level bureaucrats and senior officials controlling revenue streams and administrative choke points. Even the “integrity pillars” that are supposed to impose checks and balances – from the courts to the supreme audit agency – may be implicated. It is not unknown for interest groups and civic associations to be compromised as well:

In the worst performing developing countries, the dominant organizations of civil society are deeply implicated in the political impasse and in the redistributive pressures which have prevented accumulation and growth.

³ See Thomas and Meagher (2003) for a review of literature in this area.

⁴ Jain (2001: 72).

*Presenting the problem as one of bad states which have to be disciplined by good civil societies fundamentally misrepresents this historical reality.*⁵

DYNAMICS

What causes corruption to change? In other words, how can we explain a rise or fall in the level of bribery and theft, the emergence of new forms of graft, the spread of corruption into new activities and populations, or a major downturn in the corruption level? Despite its importance, the question of dynamics has not been thoroughly researched, and there is no real consensus. A few major themes do emerge in the literature on corruption dynamics:

1. The importance of balance. Johnston (1997) puts corruption into a comparative framework in order to shed light on its political impacts: for example, does it support political stability, galvanize movements for reform, or lead to violence and collapse? In an effort to explain these disparate effects, he puts forward the concept of “sustainable democracy.” This concept looks beyond the existence of liberal political and economic institutions to the “existence of multiple and broadly balanced political forces.” The balances involved here are:

- between the *accessibility* and *autonomy* of political elites, i.e., while private interests can influence policy, officials are able to formulate and carry out policies authoritatively; and
- between wealth and power, i.e., both political and economic paths of advancement are sufficiently numerous and open that trading wealth for office (or vice-versa) is not a serious temptation.

When these factors are in balance, corruption remains under control and does not destabilize politics; a serious imbalance in either of these factors fosters corruption. Particular combinations of imbalances give rise to characteristic systems and problems of corruption. Moreover, these situations are dynamic, with social ferment, economic change, and political contention shaping opportunities and influencing where society draws the line between the state and the market, and between acceptable and unacceptable influence.

2. The destabilizing influence of major change. Corruption appears to move in patterns analogous to those of crime, disease, manners, and financial markets. There seem to be periods of stable equilibrium and other periods when the equilibrium becomes unstable and shifts. The latter include periods of rapid social or economic change, consolidation of new regimes, and successful anti-corruption campaigns. The late 19th-century “Gilded Age” in the US and the period from late communism through early transition in Russia, for example, were both periods of rapid change and proliferating opportunities. These changes apparently led to substantial increases in the amounts and forms of corruption.

A high level of corruption appears exceedingly difficult to reverse. A high-corruption equilibrium is likely to shift downward only as a result of the accumulation of many types of changes—economic, political, social, domestic and international. Rapid reversals are rare, but they do exist: Hong Kong and Singapore since the 1960s provide the leading (if somewhat idiosyncratic) examples.

⁵ Clague (2002: 12, quoting Khan 1998, emphasis in original).

3. The budget constraint. Changes in key fiscal resources and the restraints they impose can also affect the quality of governance. Scholars examining political development throughout history have stressed the importance of a regime's budget constraint in fostering change. For example, the democratic revolutions of the late 17th and 18th centuries arose to a large degree from an insufficiency of sovereign revenue sources available to kings and the consequent need to seek consent for tax levies from representative bodies. In contemporary settings of development and transition, observers have noted that "[g]overnments that are dependent on their own citizens for critical resources appear more effective at converting material resources into human development" (Moore et al. 1999). In contrast, sources of rents or money flows that do not depend on political bargaining tend to make government less accountable for expenditures, hence more authoritarian, more wasteful – and indeed more corrupt. This has often been the case with natural resource windfalls (Leite and Weidmann 1999, Wantchekon 1999). It can also happen in the foreign aid context:

Aid dependence can undermine institutional quality by weakening accountability, encouraging rent seeking and corruption, fomenting conflict over control of aid funds, siphoning off scarce talent from the bureaucracy, and alleviating pressures to reform inefficient policies and institutions.⁶

4. The normative dimension. Good governance involves adherence to laws and other rule-systems that are sanctioned by the state, at the national, provincial, or municipal level. Socialization, along with rational expectations about others' behavior, reinforces the individual's tendency to follow broadly accepted norms of proper behavior, avoiding practices clearly within the society's definition of "corruption." Individuals interpret others' norm-consistent behavior as evidencing acceptance of, and possibly support for, those norms. Should the individual be tempted, she/he would be restrained by feelings of shame derived from expectations that others will disapprove. In some cases this understanding may be false, with the result that observed behavior supports an unpopular norm that appears too costly to break (Clague 1993, Huang and Wu 1994, Bicchieri 1997). Posner (2000) interprets these dynamics in terms of *signaling*. In this view, social norms are self-enforcing because people feel compelled to signal their "type": e.g., "good" types comply with the norm. A rule-obedient person who incurs costs from proper behavior may discover that several others are violating the rule and reaping gains – in which case she/he may feel like a "sucker" and abandon the norm. Socialization, prominent examples set by leaders, and patterns of behavior can either reinforce or undermine a rule, setting off a behavioral cascade in a new direction. In some cases, a hard-core minority with commitment to a norm can block the wholesale reversal of a behavioral equilibrium and indeed initiate a move to re-establish widespread adherence to the norm (Clague 1993, Bicchieri and Rovelli 1995). Public health campaigns furnish one kind of example here, fascist and communist efforts to redirect citizen behavior another.

DIAGNOSTIC APPROACHES

"Corruption" is not a unitary or discrete phenomenon. It takes many forms, each with different mechanisms of exchange, susceptibility to discovery and punishment, and externalities – i.e., costs (or benefits) for society at large. The forms of corruption are too numerous to list here, but Table 1 presents several illustrative types.

⁶ Knack (2000). The author is indebted to Melissa Thomas for the research on this point.

TYPOLOGIES

The World Bank (2000) has schematized the forms of corruption prevalent in transition countries by identifying two broad categories based on the mechanism of exchange. *State capture* refers to the situation where individuals, groups or enterprises seek to influence the formulation of laws, regulations and policies, so as to secure special advantages. This concept refers not to lobbying per se, but to illicit provision of private gains to policy makers in exchange for informal, nontransparent and preferential channels of access to government policy making. This reflects the earlier notion of regulatory capture, in which government agencies come under the influence of regulated industries, doing their bidding in certain areas as if by reflex. Thus, for example, a Russian oligarch who controls a network of mining, energy, and banking concerns could exert a powerful influence on the Kremlin or a regional government, in essence extracting tailored policies and laws reflecting his private interests.

The concept of state capture is defined in contrast to *administrative corruption*, in which illicit favors are used to distort the implementation of existing policies. We could also call this the residual category of *ordinary corruption*. It takes such forms as:

- the exchange of bribes for the unlawful granting of licenses, state bank loans, privatization awards, court judgments, and infrastructure contracts;
- “grease payments” to secure permits, customs clearance, and government services to which the payer is entitled; and
- the misdirection of public funds by state officials for their own benefit or that of their families or friends.

The World Bank’s analysis of corruption challenges and priorities in the transition countries rests on its categorization of countries according to their level (high or medium) of these two broad types of corruption. Thus, in the high “state capture” countries, the concentrated power of economic interests obstructs reform and restricts access to policymaking processes. Moreover, a high level of state capture suggests insufficient government attention to market-oriented restructuring of the economy, in favor of dividing spoils among influential oligarchs and *arrivistes* possessing the cash to buy policies.

Apart from the forms and mechanisms just discussed, one could alternatively categorize corruption phenomena in terms of their *pattern of organization*. Analyses of the industrial organization of corruption distinguish *centralized* or hierarchically controlled corruption from *decentralized* corruption (Shleifer and Vishny 1993). This taxonomy suggests a scale running from (1) more disciplined systems of corruption that maintain basic systems of public order and support investment expectations, to (2) outright kleptocracies where theft and predation are virtually uncontrolled and unpredictable, causing serious harm to the investment climate (Rose-Ackerman 1978).

Other things equal, the latter is more disruptive and costly in economic terms. A variant taxonomy describes corruption systems as falling into one of three models, ranged along the scale of centralized discipline: Korea (especially in the 1960s-‘70s), the Philippines (especially under Marcos), or Congo (Mobutu’s Zaire) (Klitgaard 1988).

SYSTEMS

Particular acts of corruption thus have little meaning on their own – their policy implications turn on whether or not they form part of a larger *system*. Let us take as an example the exchange of a

bribe for an unjustified benefit, such as a construction contract or state bank loan. Formally, the corrupt official is betraying his political superior and the public trust. In some circumstances, this is essentially the end of the story: an official seizing a special opportunity for gain. This analysis can only hold if the political and administrative systems are relatively well-developed and autonomous, generally clean, and effectively monitored by courts and watchdog agencies. In transition countries, this is rarely the case, and we must consider another likely dimension: that this exchange of favor for bribe is not simply localized or opportunistic, but embedded in a larger system.

Acts and schemes of corruption take a host of different forms. A full understanding of the causes of such corruption will depend on accurate analysis of its political-economic features. We can simplify the key distinction as one between two categories: (a) individualistic (or purely opportunistic) corruption and (b) systemic (or organized) corruption. Depending on which of these two categories one is faced with, a different diagnostic approach will apply: either a “narrow” principal-agent or a “wider” political economy approach. Table 1 illustrates these divergent approaches with respect to eight illustrative forms or modalities of corruption.

Further, the sheer extent of corruption – whether it has spread to all, most, or a minority of public institutions – will have an important impact. Most obviously, the more widespread it is, the more universally damaging and the higher the cumulative cost of dealing with various government control points. Also, as more arms of government and institutions of public life are compromised, the fewer are left to resist it or indeed to strike back. In short, the same act of bribery means different things in different contexts: in one context, an individual’s opportunistic act; in another, one of countless such exchanges in a system that undermines checks on its growth. The latter context can be described as one of *systemic* corruption.

Importantly, as the number of people and agencies in a scheme of corruption grows, not only is more money needed for sharing, but greater investment goes to maintaining secrecy and coordination. Elaborate group arrangements of this kind are variously termed collective, institutionalized, or structural corruption – as well as organized or white-collar crime (Karklins 2002, Gong 2002). Examples include organized smuggling, collective embezzlement, moonlighting enterprises using government property, and state enterprise asset-stripping.

TABLE 1. ILLUSTRATIVE TYPES AND DIAGNOSES OF CORRUPTION

Form of Corruption	Diagnosis of Causes	
	Individualist/ Narrow Focus	Structural/ Wider View
Corporate-bank collusion to engage in fraud & self-dealing	Weak/ politicized bank supervision, flawed corporate governance, lack of transparency & criminal enforcement.	Nomenklatura-affiliated networks enriching selves and their parties/ campaigns via banks, firms, state.
Diversion of state oil revenues to personal and campaign accounts	Weak accounting and auditing systems, no controls on campaign finance or money laundering, lack of transparency & criminal enforcement.	Network control of state, parties, firms translates into state fiscal autonomy from political processes & ability to self-enrich and perpetuate control.
Bribery, fraud & collusion in customs administration	Lack of transparency, monitoring & audit, control (e.g. via computers) of valuations & levies; low official pay & professionalism; incentive effects of high duties.	Patronage system requires bureaucrats to buy positions and pass bribe shares upwards. Imbalances mean government is main employer & can impose will on traders. Trade reform would threaten status quo sustained by elite collusion, lack of political competition, and reliance of campaign funds on corruption.
Procurement and infrastructure: bid-rigging, kickbacks, over-invoicing	Vague design parameters and bid procedures; weak inspection and audit; no competition; no bid protest procedures in place	Elite and mafia networks embedded in state and private sector institutions engage in collusion and self-enrichment; weak corporate governance & absent/inadequate official asset declarations; campaign finance dependent on bribery
Judiciary and prosecutors: bribery and favoritism	Low judicial status and pay; no checks and balances in appointments/tenure; vague laws and procedures; ineffective appeal system, oversight, sanctions	Lack of real political challenge/ competition; weak norms of legality and accountability; carry-over of “telephone justice” from Soviet era; social imbalance & lack of economic restructuring mean no effective constituency for enforcement of contracts, property rights, civil liberties

Organizing these forms of corruption not only is expensive to the parties involved, but imposes potentially large negative externalities on society at large. Costs entailed in such a system include payment to superiors for protection; managing and paying a labor force to run the scheme; purchasing the silence of various collaborators; laundering operations; and the use or threat of violence against anyone threatening non-cooperation or exposure. An ambitious scheme may require the support (or blackmailing) of auditors, prosecutors and judges, and reporters – hence the active suppression of civil rights and governmental integrity.

The concepts just reviewed give us, in combination, a greater ability not only to understand and address corruption on the “micro” level, but also to put this into a meaningful context. Some understanding of this wider setting is critically important for getting at the forces that drive and maintain systems of corruption, identifying the most effective means of attacking them, addressing the trade-offs of various potential interventions, and basing strategies on a vision of how corruption might actually be reduced and brought under control over time.

THINKING STRATEGICALLY

There can be no off-the-shelf “strategy” to combat corruption. One can only be created on the basis of reasonably detailed local knowledge supported by strategic thinking. What does this mean as it concerns corruption in the E&E Region? First, one needs a conceptual framework for understanding and assessing corruption issues. We discussed the main elements of this in previous section. Second, this must be brought together with thorough understanding of the country or context at issue. Mission staff, partners, and external experts can provide this. Third, a strategic framework is needed to bring these elements together in a way that generates actionable guidance for the USAID mission. In this section, we present the main features of such a framework – building on the USAID Anti-Corruption Strategy and the E&E Bureau’s TAPEE framework. In the next section, we apply the framework to a few illustrative scenarios, showing how strategies can be generated.

HOW TO COMBAT CORRUPTION

In order to think about how USAID can help reduce corruption, one must first have some historical idea of how societies have reached the desired end-point of sustained low corruption. What influences have brought corruption under control? We need some general corruption control theory on which to hang more specific USAID anti-corruption strategies. Just as Part 2 suggested that “corruption” is not a single, specific activity, there is similarly no universal corruption antidote. The strategy must differ depending on (a) the extent to which the corruption is systemic; (b) the extent to which broader political and socio-economic trends favor anti-corruption reform; (c) the location(s) and form(s) in which the corruption arises; and (d) the estimated costs and benefits of the anti-corruption campaign – in the broadest sense.

Recall the distinction made previously, between individualistic and structural diagnoses of corruption problems. Some corruption phenomena are simply matters of individual opportunism, while others are embedded in a larger parallel structure of governance and exchange.

The choice of diagnostic approach is critically important not only to interpret patterns and causes of corruption, but also to design a response. Individualistic approaches generally lead to technocratic responses – designed to cope effectively with single-agency or opportunistic corruption in an otherwise sound governance scenario. Systemic corruption, however, implies compromised institutions of governance, and thus calls for broader political and economic reform efforts. Table 2 briefly summarizes the differing approaches needed in responding to corruption, in settings with varying levels of corruption and institutional quality.

If a wider structural analysis shows corruption to be systemic, what should be done? In practice, how can more widespread or entrenched corruption be overcome? In Part 2, we discussed corruption dynamics. Successful responses make use of dynamic pressures, crafting policies and seizing opportunities created by periods of change in order to strengthen anti-corruption forces and to push the level of corruption down.

TABLE 2: COMBATING CORRUPTION IN DIFFERENT SETTINGS

Corruption Reach/ Institutional Context	Individualist	Structural/Systemic
Strong state autonomy & rule of law/ developed countries	Technocratic reforms can succeed	Success possible, but requires combined political <i>and</i> technocratic reforms
Weak state autonomy & rule of law/ developing & transition countries	Technocratic reforms might succeed, but with difficulty	Success doubtful, absent regime change and systemic political reform

Historically (in open societies), successful anti-corruption reforms have necessarily occurred in a receptive political environment shaped by crisis or by widespread perceptions that long-term trends call for fundamental change. For example, change might follow one of these patterns:

1. The problem is recognized, defined, and addressed as a policy matter, where it has not been before. This could be the result of long-term social and economic change.
2. A change in personnel or attitude in a key branch of government or agency of restraint ushers in an effective crackdown or reform. This assumes fairly widespread support or acceptance.
3. Major proposed changes in government structures and restraints are approved and implemented after a long campaign or in the wake of scandal. Again, wide acceptance, perhaps in the wake of social and economic change, makes this work.
4. Crises or economic instability cause mass discontent, eliciting elite response and political change. Here, too, long-term changes may have changed expectations, increasing the demand for reform.

It is worth emphasizing the *political* nature of these reform processes. Aid agencies and international financial institutions have reason to dissociate themselves from direct intervention in domestic politics. (In the case of the World Bank, this is a legal requirement of its charter; and although USAID is less constrained in formal terms, non-partisanship seems to be viewed as important to its credibility.) As a result, anti-corruption and other reform programs are often presented as technocratic measures.

For example, the World Bank's (2000) "Multi-pronged Strategy" for addressing state capture and administrative corruption in transition countries calls for action on five fronts:

- Institutional restraints (e.g., independent judiciary)
- Political accountability (e.g., competition and transparency)
- Competitive private sector (e.g., restructuring and lowering entry barriers)
- Public sector management (e.g., civil service and expenditure control reform)
- Civil society participation (e.g., freedom-of-information initiatives)

This approach adds political and economic competition to the factors cited in the TAPEE framework (in this, the World Bank and the overall USAID Anti-Corruption Strategy are in agreement). Such objectives would in principal be relatively uncontroversial in many Western industrial countries. However, in many transition settings – and especially those suffering from systemic corruption – these are bound to be highly contentious. The necessary reforms imply a large transfer of power and earning opportunities away from specific groups, in return for seemingly diffuse good governance benefits for society as a whole.

Historically, reform of this magnitude has not often come about for the reasons put forward in the donor agencies' anti-corruption rhetoric. Institutions – meaning the “rules of the game” in effect – are created and reformed in response to crises and clashes of societal interests such as classes, industries, and movements. Scholars have described governance institutions from ancient Rome to the contemporary US as equilibrium solutions to repeated conflict. Thus, for example, the English constitutional settlement of 1689 came about as a stable resolution of repeated conflicts among church, class, and commercial interests. It succeeded because the multilateral commitments that underlay it were credible and mutually enforcing, and the system as a whole could sustain itself (Bates et al. 1998). Similarly, sustained anti-corruption reforms, such as the professionalization of the federal civil service in the US during the late 19th century, or the establishment of Hong Kong's Independent Commission Against Corruption in the 1970s, required credible and enforceable commitments by business interests, party hierarchies, and other interested parties.

In short, good ideas for improving governance carry a certain weight, but they create enduring institutions only by serving to resolve repeated political conflict to mutual advantage. By implication, successful USAID anti-corruption interventions are far likelier to be based on political than technical merit.

In particular, tackling specific forms of corruption is only in part a matter of redesigning administrative relationships. As we have suggested, corruption schemes respond to issues arising in the broader political, social, and economic arena. Hence, any sustained solution to a corruption problem must also be sought there. For example, the need for political campaign finance lies behind many organized forms of corruption. In many transition and developing countries, politicians may turn to state institutions such as revenue agencies (e.g. customs), public works and procurement departments, or state-owned banks as sources of campaign funds. Other things equal, cracking down on particularly corrupt sectors may simply cause campaign finance-related corruption to migrate to other areas.

What are the strategic implications of these insights for USAID? Taking the illustrative forms of corruption mentioned in Table 1, Table 3 suggests some illustrative approaches to diagnosis and treatment of these problems. The two categories of response are best viewed as complementary rather than mutually exclusive.

TABLE 3: ILLUSTRATIVE RESPONSES TO CORRUPTION

Forms of Corruption	<u>Responses</u> ⁷	
	Technocratic (individualist)	Political (structural)
Corporate-bank collusion to engage in fraud & self-dealing	Strengthen & tighten bank supervision, corporate governance, <u>transparency</u> & criminal <u>enforcement</u> .	Restructure bank & firm ownership, increase FDI, tighten regime budget constraint, increase political & economic competition.
Diversion of state oil revenues to personal and campaign accounts	Strengthen & tighten accounting and auditing (accountability) systems, controls on campaign finance & money laundering (<u>prevention</u>), <u>transparency</u> & criminal <u>enforcement</u> .	Improve <u>transparency</u> & competition, reduce control rights to cut corrupt linkages. Tighten regime budget constraint, coordinate external agents to signal zero tolerance (<u>education</u> , <u>enforcement</u>). Support SME growth.
Bribery, fraud & collusion in customs administration	Tighten administrative controls, improve civil service conditions, reduce & rationalize duties (<u>prevention</u>).	Restructure political & economic systems to promote competition, support campaign finance reform (<u>transparency</u> , <u>prevention</u>), encourage export-oriented SME growth.
Procurement and infrastructure: bid-rigging, kickbacks, over-invoicing	Tighten design parameters and bid procedures; introduce competition (<u>prevention</u>); strengthen inspection and audit; put bid protest procedures in place (<u>accountability</u>)	Tighten regime budget constraint, increase political & economic competition; increase <u>transparency</u> ; strengthen corporate ownership incentives & governance; introduce official asset declarations and campaign finance reforms with robust monitoring mechanisms (<u>transparency</u>)
Judiciary and prosecutors: bribery and favoritism	Improve judicial status and pay; introduce checks and balances in appointments/tenure; revise & sharpen laws and procedures (<u>prevention</u>); strengthen appeal system, oversight, sanctions (<u>transparency</u> , <u>accountability</u>)	Strengthen political competition; influence norms (education) of legality and <u>accountability</u> ; intensify economic restructuring and shared growth; foster constituencies for enforcement of contracts, property rights, civil liberties

USAID: ANTI-CORRUPTION ROLE AND STRATEGY FORMATION

What should a USAID strategy in the anti-corruption area actually be designed to *do*?

Discussions in this area often begin with a listing of the “integrity pillars” that characterize well-governed countries (e.g., independent judiciary and supreme audit agency), identifying this array as the desired end-point. Two problems arise here. First, the integrity pillar approach generates a long list of reforms, without providing a political-economic “roadmap” for their achievement. Second, there will often be existing programs – whether supported by USAID or by others – addressing many if not most of these broad reforms. An anti-corruption strategy may reinforce the urgency of such reforms, but will otherwise not add much value in terms of marshaling scarce resources.

⁷ Note that the elements of the E&E Bureau framework – TAPEE – appear in both the ‘technocratic’ and ‘political’ columns, though predominantly the former. This underlines the complementarity of the two approaches, and the importance of setting the TAPEE framework within a broader understanding of political-economic driving forces.

How can USAID missions become truly *strategic* in their choices? The TAPEE framework is a good starting point, when used in a careful, context-specific way to set priorities. When combined with the “structural” perspective discussed above, TAPEE can provide a roadmap for using USAID resources to move away from a low-TAPEE, high-corruption scenario towards a higher-TAPEE, lower-corruption end-point. In the discussion that follows, we propose a set of guidelines to meet this need (a kit for creating country-specific roadmaps, if you will).

STRATEGIC FOCUS

In thinking about anti-corruption strategy, we can draw an analogy to the internal strategy, coordination, and policy development processes of a country (or province or city). These processes tend to center first on defining and measuring the problem, using this to inform and gain consensus on priorities. In the anti-corruption area, sometimes scandal and crisis create a sense of urgency. The focus then shifts to what measures are to be put in place, with what instruments, by what organization(s), and with what resources. As in any important field of policy, problems and solutions overlap ministries and jurisdictions, requiring a multivalent and coordinated response. The scope and timeframe of the response need to be spelled out: enforcement only, or diagnostic studies as well? Responsiveness to complaints, or proactive long-term planning and restructuring? If a lead agency is needed, is this an existing unit or a new special-purpose agency? Key questions of institutional credibility must be considered. Is the government or parliament truly committed to restraining corruption? Will the approach be even-handed, the gains and losses equitably shared?

Reform strategies gain credibility by showing that they are new and different. In a sense, the medium is the message. If we created checklists of what anti-corruption activities were being carried out pre- and post-strategy, it is possible that they would not look dramatically different. Where effective strategies and initiatives have been mounted, the key elements of success may be essentially procedural: heightened recognition, consensus-building and prioritization, new agencies and/or mechanisms of inter-agency coordination, and some concentration and augmentation of resources. The courts, auditors, civil service, parliamentary committees and other structures remain, but the effort has become more focused, and a message has gone out that things will be different. This is not to suggest that anti-corruption campaigns and commissions are always successful – far from it. Rather, where these and similar initiatives succeed, they do so by bringing new focus, coordination, and commitment. These efforts gain credibility through some combination of high visibility, increased investment, checks against partiality and backsliding, and taking on the tough issues.

How does this apply to USAID missions? They do not, of course, exercise direct control over host-country policies or institutions. Rather, they can influence that environment and fund activities within it. Thus they are players (often important ones) within their host-country policy environments, but they are not policymakers as such. Also, as part of the U.S. Government and of the international donor community active in the host country, USAID missions participate in two additional axes of influence. An anti-corruption strategy will therefore involve (a) influencing the host country policy environment in ways that help restrain corruption, (b) influencing and coordinating with other members of the USG and donor community to use their programming and influence in mutually supporting ways, and (c) tailoring USAID’s own portfolio, and particular sectoral programs, to advance anti-corruption goals.

One aspect of any USAID Mission’s strategy development would entail examining the relevance of corruption to overall program priorities, values, and strategic objectives. Corruption in many USAID/E&E countries touches a wide range of areas and imposes a host of different costs. Which are the ones that the USAID Mission cares most about? The literature on corruption

provides no firm basis for identifying the “costliest” forms of corruption. However, it does provide some guidance as to the kinds of harm that certain types of corruption may create, and suggests how serious these harms may become, based on prior cases. A USAID Mission can tailor its anti-corruption strategy to address the harms that it considers to be the highest priority – e.g., harms to political stability, economic development, or social equity. Moreover, a careful analysis will indicate the approximate relative costs and benefits of attempting to address certain forms of corruption – versus *not* addressing them. Table 4 provides an illustrative (and much abbreviated) cost-benefit analysis of potential responses to the eight forms of corruption introduced in Table 1. (This is not meant to suggest a *specific* type of analysis. Depending on the situation and the resources at hand, a number of analytical approaches might be appropriate: cost-benefit, risk-benefit, force-field, SWOT, etc.) Tables 1-4 are aggregated into a summary table in Annex 2.

TABLE 4. RESPONSES TO FORMS OF CORRUPTION – BENEFITS AND COSTS

Form of Corruption	Cost-Benefit Issues	
	Status Quo	Effective Response
Corporate-bank collusion to engage in fraud & self-dealing	<p>Misallocates capital, deters investment, threatens stability of financial system, feeds crony/ criminal networks, drives rent-seeking and further weakening of corporate governance.</p> <p>Exchange of illicit gains may enhance short-term stability and elite consensus.</p>	<p>Correcting this enables effective corporate & financial sectors, hence sustained & balanced economic growth; cuts crony/ criminal networks off from this source of support; discourages rent-seeking.</p> <p>Direct attack on corruption may backfire; restructuring takes time, political capital & sustained policy focus, and provokes opposition; short-term economic disruptions; who will take the lead?</p>
Diversion of state oil revenues to personal and campaign accounts	<p>Wastes public revenue, fosters unsustainable natural resource use, feeds crony/ criminal networks, undercuts political competition, drives further corruption & political repression.</p> <p>Exchange of spoils may enhance short-term stability and elite consensus.</p>	<p>Correcting this will free up revenue for public good investments, remove serious policy distortions and motives for repression, and loosen constraints on political competition.</p> <p>Crony/criminal networks will fight back; change requires big efforts on oil sector restructuring and campaign finance reform; near-term disruptions, possible instability.</p>
Bribery, fraud & collusion in customs administration	<p>Deters trade and investment, encourages smuggling, harms revenue effort & balance of payments, penalizes trading and transport firms, imposes a drag on economic growth, fuels patronage systems & political monopoly, drives further corruption & rent-seeking.</p> <p>Exchange of spoils may enhance short-term stability and elite consensus.</p>	<p>Correcting this will encourage trade & growth, enhance revenues, enable a more professional public service, loosen constraints on political competition.</p> <p>Patronage networks will fight back, seek alternative spoils; change requires customs, civil service, and administrative law reforms.</p>
Procurement and infrastructure: bid-rigging, kickbacks, over-invoicing	<p>Results in lower quality public goods and infrastructure at higher cost; creates public hazards; distorts public investments; fuels political monopoly & cronyism; undermines state control systems; drives further corruption & crime.</p> <p>Exchange of spoils & contracts may enhance short-term stability and elite consensus.</p>	<p>Correcting this will improve public investments, enable more political competition and shared growth, remove a motive to undermine state control systems, reduce benefits to crony/ crime networks.</p> <p>Change requires confronting strongly entrenched networks & patterns of doing business, hence taking away concentrated benefits, for diffuse results.</p>
Judiciary and prosecutors: bribery and favoritism	<p>Undermines autonomy & professionalism of judicial sector; distorts decisions and fosters further corruption; results in impunity, injustice, repression; creates political backlash; dampens economic growth.</p> <p>Exchange of spoils & favors may enhance short-term stability and elite consensus.</p>	<p>Correcting this will defuse resentment, encourage investment, foster public order & protection of civil liberties, enhance efficiency of courts.</p> <p>Change requires some basis for the rule of law; reform may be highly politicized and difficult; parallel efforts needed in reform of constitution, judicial administration, pay & conditions, appeal & oversight, training.</p>

TAKING AID EFFECTIVENESS INTO ACCOUNT

It is critically important to distinguish the role of an aid donor agency from that of a host-country actor, such as a branch of government, a policymaker, or a reform advocate.

Donors have special capabilities – and limitations – that other actors do not. For example, donors' resources enable them to affect the political equation, to support favored policies. Brautigam (1997) offers several recommendations on the role of aid in reform, including the following:

- The need to compensate losers from reform, using both social safety nets and “pork, patronage, rents and spoils to maintain support for their initiatives.” (p. 18)
- “Policies and programs that create winners before creating losers, or that deliberately accelerate the gains to winners, ease the task of creating constituencies for reform.” (p.19)

Donors also do well to remember that supporting particular constituencies can have unpredictable results – and that all the risks will be borne by those constituencies.

Also, aid effectiveness is subject to significant constraints. Adverse selection problems are severe: studies consistently show that the countries most likely to succeed need external aid the least, and those with greatest need are unlikely to make good use of aid. Further, aid is fungible. A World Bank (1998) study on aid effectiveness states (p. 74): “The safest assumption for donors is that they are, more or less, financing whatever the government chooses to do.” Indeed, the literature suggests a *negative* relationship between the size of “soft” money inflows (e.g., natural resource rents, foreign aid) on the one hand, and the quality of governance on the other hand. This is consistent with the historical linkage of democratic change with fiscal constraints (i.e., where raising taxes requires a vote), and with the influence of hard budget constraints on the quality of economic restructuring in transition countries. It is undoubtedly the case that in many transition countries—especially those most dependent on aid and natural resource revenues—the net effect of high financial inflows (including aid) is to defer reform and encourage corruption. Additionally, donor aid for institutional reform purposes is especially subject to principal-agent difficulties, reflecting the diverse interests and incentives of donor and recipient organizations (Murrell et al. 2002).

In virtually no case can USAID reverse a situation of governance failure unilaterally. The issues are: how much leverage does USAID have, and how can it make best use of it. Since USAID is not really a free agent, and since it must accept the situation in a country as given, its leverage is mostly pre-determined (exogenous). At the same time, USAID can strategically marshal its resources to influence its posture and leverage.

What are the instruments available to USAID for purposes of addressing corruption? The range includes: donor and USG-level policy coordination; withholding support from a recalcitrant government and directing it to NGOs; protecting USAID sectoral programs from the direct influence of corruption; supporting basic long-term restructuring and reform; pursuing “upstream” governance improvements such as administrative reforms; and finally, direct anti-corruption initiatives such as support for audit or detection systems.

TAILORING STRATEGIES: VARIABLES IN THE COUNTRY PROGRAM ENVIRONMENT

There can be no strategy in the abstract, but only strategies that respond to particular contexts. Thus, a strategic framework must incorporate a methodology for taking key situational variables into account in the formation of strategies. In Part 2, we considered methodologies proposed by the World Bank (2000) and Johnston (1997). Following is a summary of our proposed methodology, which builds on these previous efforts (a more detailed presentation appears in the Annexes). In Part 4, we illustrate its use by adapting it to some sample scenarios.

We propose four groups of variables that capture the main corruption-relevant features of any country environment in which USAID programs operate: (See Annex 1 for more detail.)

1. Governance Capability. Key capabilities for effective governance include the socio-economic characteristics of the society and its elites; adherence to the rule of law; and the openness of the political regime. The component variables can be summarized as follows:

- **Governing regime quality.** This comprises stability and order, commitment to the rule of law, and a developmental ruling elite.⁸
- **Social and political balance.** This includes social capital, pluralism, equivalent economic and political opportunities, and norms of integrity.⁹
- **Political openness.** This deals with civic and political freedoms, information transparency, and democratic governance.

The higher [lower] the overall value of these governance variables, the more [less] likely it is (*ceteris paribus*) that reforms will take place either indigenously or in response to aid interventions, that reforms once adopted will be implemented and sustained, and that governance will improve significantly in the near to medium term. In terms of the transition region, we are likely to encounter high values on these variables in parts of Central and Eastern Europe, low values in the slow reformers of the ex-Soviet Union, and medium values in the countries (and provinces) across the region that have experienced a mix of reform advances and reversals.

2. Corruption Remediability. This cluster of variables concerns the quality of governance structures in the public and private sectors and the intensity and remediability of corruption problems. The variables comprising this cluster are:

- **Integrity of governing institutions.** Here, we are concerned with the autonomy of such agencies of restraint as courts and audit agencies, the professionalism of the civil service, and the quality of official responses to corruption.

⁸ An elite can be considered “developmental” if its self-interested behavior is consistent with shared economic growth and increasing welfare. This will be the case where increasing prosperity poses no threat to the elite’s maintenance of its political power – i.e. where economic and political cleavages are not so strong as to create opposition to developmental policies (Robinson 1997).

⁹ This approximates Johnston’s (1997) concept of political balance supporting sustainable democracy.

- **Quality of private sector governance.** This relates to the quality of corporate governance, the competitiveness of the private sector, and its autonomy from the state.¹⁰
- **Scope and entrenchment of corruption.** This deals with the extent of corruption: how far it has spread, what agencies are compromised, and how organized and entrenched the corruption is. It is negatively correlated with the overall corruption remediability variable.¹¹

The higher [lower] the overall value of this variable, the greater [lower] likely the likelihood of success for direct or technocratic anti-corruption efforts and donor interventions in this area. The variable essentially measures the country's ability to avoid corruption spirals and to redress the corruption problems that do occur. We would expect this value to be relatively high in the first round EU accession countries, medium in Eastern Europe, and low in most other countries in the region.

3. Reform Leverage. This group of variables relates to a governing regime's incentives to reform and to rein in corruption. The component variables are:

- **Strategic value.** This variable concerns the country's perceived economic, political, and strategic importance to outsiders such as the US – including its role in regional security. (It has a negative correlation to overall leverage.)
- **International integration.** This is the extent of participation in global and regional arrangements (e.g., the EU and NATO), and involvement in international commerce.¹²
- **Budget stringency.** Here we focus on the importance of fiscal sources (e.g., mineral rents or foreign aid) that tend to weaken expenditure discipline, as compared to budget constraints that tend to reinforce it.¹³
- **Developmental constraints.** There are a range of these, including crisis, conflict, and social norms that obstruct effective governance. (It has a negative correlation to overall leverage.)

¹⁰ See Black et al (1999) and Root (1991) for analysis of the link between state direction and control of economic sectors, on the one hand, and incentives for corporate rent-seeking (often associated with corruption) on the other hand – with examples from transition Russia and 18th century Europe.

¹¹ This would include the relative extent of state capture and administrative corruption (World Bank 2000).

¹² See Martin (2002) and Meagher (2000) on the importance of international regime membership (actual or potential) in encouraging governance-optimal policy choices.

¹³ See Lewis (1996) for an analysis of how the increasing influx of oil revenues during the 1980s and 1990s helped transform Nigeria's military governments from corrupt oligarchies to essentially unrestrained predators, using control of offices, security services, and repression to further their personal enrichment. Suggesting that budget constraints are helpful in governance terms is different from asserting that donor financial leverage is important. Both Clague (2002) and Killick (1998) are skeptical of donors' ability to use financial leverage to bring about reform.

These factors influence the overall likelihood of reform, based on the leverage available to domestic reformers, international organizations, and donor countries. The higher [lower] the value of reform leverage, the greater [lesser] the impact we can expect from an aid program investment (other things equal). We would expect to find lower values in resource-rich or strategically important countries, and higher values in countries moving into the EU, NATO, and significant participation in the international economy.

4. USAID Influence. This set of factors concerns the posture of USAID in a given country, i.e., USAID's relationship to other donor programs, its influence on the coordination of overall US policy in the country, and the extent to which its existing programming trends are supportive of anti-corruption objectives. These variables are:

- **Donor coordination.** How consistent are the IFIs and bilaterals regarding aid generally and corruption in particular, and what is the extent of competition and conflict among their approaches.
- **Coherence of U.S. Government aid policy.** Here, we are concerned with consistency among US agencies involved in aid, both generally and with regard to corruption.
- **USAID resources and focus.** This variable reflects USAID's level of funding in the country, the priority and focus it places on corruption, and its ability to keep this focus and use it to press for reform.

High values here translate into significant overall influence, hence the ability of USAID to pursue a consistent anti-corruption strategy with minimal conflict among donors and US agencies, and with sufficient resources. We expect high values in countries where the US is the main Western donor country, and where conflicts among economic and strategic priorities are absent or well-managed. This tends to be true especially of smaller countries outside the first-round EU accession candidates.

DESIGNING COUNTRY STRATEGIES AND PROGRAMS

What are the implications of the preceding discussion for USAID strategizing and programming in this area? We have suggested that there can be no “strategy” in the abstract. We present rather a framework for generating corruption-relevant program strategies in divergent country contexts. First, we suggest what the process of developing a USAID mission anti-corruption strategy might involve. Next, we bring the contextual factors presented earlier into a series of fictional country scenarios, as a way of illustrating the range of situations to be addressed. A review of these scenarios suggests what an effective policy and response by the donor community would entail in each case. Following this, we look more closely at one of the illustrative scenarios, generating some strategic responses to particular forms of corruption. Last, the discussion focuses on another of the scenarios, for the purpose of reviewing the USAID mission’s full portfolio in light of anti-corruption strategy concerns.

STRATEGY DEVELOPMENT AND PLANNING PROCESSES

Effective strategizing in this field demands an inclusive perspective and process. Corruption opportunities, modalities, and systems can change quickly in response to economic growth, political shifts, crises, and reforms. Also, there is no sector of governmental, economic, or social activity where corruption cannot intrude. This suggests that anti-corruption strategy must be both multi-sectoral and inter-temporal.

In countries with relatively strong governance, corruption is largely individualistic, and such corruption systems as exist are usually localized, sector-specific, or limited to certain elements of the political universe. In the weak governance countries, by contrast, corruption touches a far larger array of sectors, activities, locations, and groups. Anti-corruption strategy needs to keep in view as full a range of concerns as possible, and in order to do that, it is best formulated jointly by all major stakeholders. This is the rationale for government-wide corruption strategies and public-private integrity plans. Similarly, major international actors—donor governments, aid agencies, and ideally the investor community as well—need to frame a common strategy. The protean nature of corruption, which thrives on ambiguity and coordination failure, calls for a common and consistent approach in bringing it under control.

Similarly, the dynamic aspect of corruption requires not only coordination by the supporters of reform, but an awareness of trade-offs, interactive effects, and temporal sequencing. Potential trade-offs are many. Reform, transition, and development at times necessitate the sacrifice of some goals – such as optimally restraining corruption in the near term – for longer-term goals such as restructuring, privatization, and liberalization. Further, it is an unfortunate reality that donor countries often pursue diplomatic, security, and transnational economic policy goals to the detriment of anti-corruption objectives. Only a joint undertaking by interested parties—e.g., USAID, other elements of the USG, the IFIs, and other donor countries—can achieve a shared perspective on priority objectives and trade-offs. Otherwise, trade-offs will be made implicitly, unwittingly, or inconsistently. These issues must also be clarified and consistently addressed within the USAID portfolio. If, for example, a health crisis requires measures that are likely to

stimulate corruption in the short term, this kind of trade-off is best made explicitly and in a way that permits the undesirable effects to be dealt with down the line.¹⁴

Efforts in this area can aim for improvements in the short, medium, or long term, and can follow either a direct or indirect approach. Directly addressing corruption in the short term may be impossible, or may conflict with long-term restructuring efforts that would have a larger cumulative effect in reducing corruption. A corollary is the need to place appropriate priority on *vulnerabilities*, especially where emergent trends may lead to runaway corruption or the entrenchment of corruption systems. Such vulnerabilities may include the continued intermingling of elite, state, enterprise, and banking interests – for example, in the form of large or monopolistic financial-industrial groups. This sort of emerging trend might pose a more serious corruption threat—whether or not it currently involves much actual corruption—than some existing forms of corruption, such as particular campaign finance abuses. In other words, a dynamic view might focus on the emergent trend as one that could lead to far more widespread, damaging, and intractable corruption than the forms that are currently extant.

Also, reflecting the analysis presented above, our strategic recommendations cover corruption phenomena that may be either individualistic or structural in their genesis, and either localized or systemic in their reach. This means using varied approaches, some of them in combination, to address different forms, systems, and contexts of corruption. It is also important to keep the *objective* of any anti-corruption initiative in mind. The ultimate objective, of course, is to constrain the reach and impact of corruption overall, and for this purpose we have stressed the need to supplement mainstream approaches with structural analyses and systematic responses.

In order to mount an effective response, USAID and its partners need to find an “entry point” – as an opportunity or leverage point that comes into view as a result of political and economic changes. Examples would include the external pressures of EU and WTO accession, the fallout from a severe financial crisis, the needs associated with negotiating an internal peace accord or political charter, and the desire to meet the criteria for special facilities such as the Millennium Challenge Account.

Realistically, however, a robust systematic response is not always possible. Resources may be too constrained, corruption too entrenched, or competing priorities too urgent to allow for this. In such situations, only lower-profile activities are possible. These activities can be designed to emphasize anti-corruption themes, mount localized institutional reforms, and demonstrate anti-corruption responses in action. Especially relevant in this context are programs that reinforce the TAPEE factors wherever possible. Activities consistent with these themes might be free-standing or they might be embedded in a program focusing on, e.g., the health or education sector. These kinds of activities can educate, demonstrate, even motivate people in government, the private sector, and civil society in ways that support anti-corruption goals. They also help to produce small reform victories that can be extended and replicated beyond the original context. The discussion below incorporates these elements as well.

ILLUSTRATIVE COUNTRY SCENARIOS

The four country scenarios in this section incorporate the variables discussed in the previous section. The scenarios are as follows:

¹⁴ Table 4 above provides an illustrative anti-corruption cost-benefit matrix relevant to these trade-offs.

- “Balkania,” a country in Southeastern Europe striving for EU accession
- “Caucasia,” a former Soviet republic in a region torn by conflict
- “Oligarchia,” a large former Soviet nation where powerful regional and economic interests vie for authority and resource control
- “Kleptokrastan,” a mineral-rich Central Asian republic

These scenarios do not purport to work out all possible value combinations, but rather present situations likely to be *typical* of transition country settings in which USAID/E&E operates. Moreover, these scenarios are all highly simplified and schematic—an actual planning process would yield a much more complete and nuanced picture. We begin with brief summaries presented in chart form. Next, we go more deeply into one of the scenarios, drawing out in a preliminary way some strategic implications for donor programming.

TABLE 5: SUMMARY USAID E&E REGION SCENARIOS		
BALKANIA		
Program Environment	Strategic Considerations	Strategic Targets
<i>High</i> Governance Capability <i>Medium</i> Corruption Remediability <i>High</i> Reform Leverage <i>Medium</i> USAID Strength	<i>Vulnerabilities:</i> State, enterprise, banking interests mingled; mafia & trafficking; state-economy imbalances <i>Entry points:</i> EU accession process; budget stringency; pressure to reduce unemployment <i>Trade-offs:</i> ¹⁵ Rebuilding state banking & welfare structures vs. attacking patronage & illicit political finance <i>TAPEE elements to emphasize:</i> accountability, prevention, enforcement	Further reforms in civil service, public finance, procurement, judiciary, electoral systems Greater transparency in political financing Trade and financial sector integrity Effective responses to white-collar and organized crime Strong partnerships with civil society Employment growth

¹⁵ See Table 4 above, and associated text, for illustrations of cost-benefit analysis pertaining to anti-corruption trade-offs.

CAUCASIA		
Program Environment	Strategic Considerations	Strategic Targets
<p><i>Low</i> Governance Capability</p> <p><i>Medium</i> Corruption Remediability</p> <p><i>Low</i> Reform Leverage</p> <p><i>Medium</i> USAID Strength</p>	<p><i>Vulnerabilities:</i> Severe imbalances due to instability & conflict, low growth & living standards, slow restructuring; mafia and irredentist interests in illicit trade; politically dominant clans & networks assert state control over the economy</p> <p><i>Entry points:</i> Need for outside economic and security assistance, U.S. as counterweight to other powers in region</p> <p><i>Trade-offs:</i> Predominance of stability & security concerns slows political and economic reform, encouraging spread of corruption</p> <p><i>TAPEE elements to emphasize:</i> accountability, prevention, education</p>	<p>Build capacity of public administration</p> <p>Develop instruments for financial management</p> <p>Encourage civil society</p> <p>Stronger public order & security Economic restructuring & growth</p> <p>Improve civil servant status, conditions</p> <p>Strengthen external watchdogs and citizen-driven accountability mechanisms</p>

OLIGARCHIA		
Program Environment	Strategic Considerations	Strategic Targets
<p><i>Medium</i> Governance Capability</p> <p><i>Low</i> Corruption Remediability</p> <p><i>Low</i> Reform Leverage</p> <p><i>Low</i> USAID Strength</p>	<p><i>Vulnerabilities:</i> Fiefdoms created by oligarchs, regional governors in league with captive industries or natural resource firms, oligarch-backed conglomerates include banking & media companies</p> <p><i>Entry points:</i> Desire of center to discipline regions and improve linkages West & East</p> <p><i>Trade-offs:</i> <i>Strengthening anti-corruption capabilities of state institutions may encourage abuses; further decentralizing may lead to more uncoordinated corruption; all sectors subject to capture by elites</i></p> <p><i>TAPEE elements to emphasize:</i> transparency, accountability, education</p>	<p>Broaden formal channels of access to the state</p> <p>Deconcentrate economic power through competition and entry</p> <p>Enhance oversight through participatory strategies</p> <p>Strengthen corporate governance quality, campaign finance transparency</p> <p>Build institutional checks into center-regional rivalries</p>

KLEPTOKRASTAN		
Program Environment	Strategic Considerations	Strategic Targets
<i>Low</i> Governance Capability <i>Low</i> Corruption Remediability <i>Low</i> Reform Leverage <i>Medium</i> USAID Strength	<i>Vulnerabilities:</i> Mineral rent dependency supporting autonomous & predatory elite with direct interests in banking and large enterprises; elite media and court system control; restricted civil rights <i>Entry points:</i> Need for FDI in mineral sector, security links to U.S. <i>Trade-offs:</i> Strategic and mineral extraction interests are pursued in ways that compromise governance; strengthening anti-corruption capabilities of state institutions may encourage abuses; all sectors subject to capture by elites <i>TAPEE elements to emphasize:</i> transparency, education	Deconcentrate economic power through restructuring, competition, and enhanced entry Build accountability through oversight mechanisms Collective action among countervailing interests Strengthen donor coordination, regime budget constraint, civil rights protections Find opportunities to increase transparency and to educate

These scenarios illustrate how the concepts and strategic approaches described in Parts 2 and 3 of the paper can be applied in (fictionalized) transition contexts. It is important to stress that these scenarios are offered only as illustrations of strategic processes and approaches USAID might use, not as templates or checklists to be followed. In Table 6, we show how the scenarios synthesize elements from the World Bank (2000) and USAID (2002) strategic frameworks, along with elements that we have added.

EXTENDED EXAMPLE: “BALKANIA” SCENARIO

Let us look at one of the scenarios in a bit more detail, with attention to the strategic concepts presented above.

Program Environment. In Balkania, governance capability is relatively high, with a medium level of corruption remediability. Communism and early transition left a legacy of closed elites, secrecy, predation, and low social capital and mobility. However, these were mainly temporary, and the negotiated transition, rapid opening, and civic activism enabled past social and elite capabilities to reassert themselves and grow. This has enabled relatively effective governance under a democratic political regime. Political and economic forces have struggled with modest success to achieve some relative balance, making it possible to bring the rampant opportunistic corruption of late Communism and the early transition much more under control. Still, problems remain, especially corruption arising from elite collusion and underpaid bureaucrats.

Balkania is likely to have relatively high-quality governing institutions, but not across the board—e.g., there may be weaknesses in the autonomy of some agencies of restraint, and in the quality of the anti-corruption effort. The quality of private sector governance will vary, but should be much stronger than in the early transition period— and as compared to the other scenarios. The extent and entrenchment of corruption are moderate—i.e., relatively low on a transition-country scale. This scenario suggests that corruption is a significant problem and could

get worse, but that it is highly remediable. The dynamic trend is improvement and progress toward integration with Western Europe, and the possibility of encouraging successful and sustained governance reforms is substantial, but weaknesses are significant and risks of reversal exist.

Reform leverage variables are reasonably high in Balkania. The country has comparatively low strategic value with relatively minor developmental constraints (compared with those in other sub-regions in the E&E area). The prospect of eventual accession to the EU, along with the lack of large natural resource rents or high aid dependency, encourage open trade and investment policies, resulting in high scores on integration and budget stringency (budget constraint). This combination of factors gives the international community as a whole (Europe in particular) substantial leverage to press for effective governance.

USAID's position here is moderately strong. Donor coordination is low, due to the strong interests of the European Union and the EBRD, in competition with USAID and the World Bank Group. US government coordination is relatively high due to a shared understanding of problems and priorities, such as illicit trafficking and money laundering, but Justice and Treasury take the lead in this area. USAID anti-corruption capabilities are relatively low as a result of both interagency division of labor and the priority that local policymakers and reformers place on relations with the EU.

Strategic Considerations. We begin with vulnerabilities. These include murky interconnections among elites, the state, enterprises, banks, and the mafia—as well as economic imbalances that encourage sale of offices and administrative corruption. What might be done to address these concerns? Coordinated efforts by the EU and other external actors can ensure a firm budget constraint on the regime, thereby keeping pressure on for early reforms such as enterprise and bank restructuring, encouragement of strategic FDI, stronger bank supervision and money laundering controls, and improved budget management leading to better balance and incentives in the civil service.

A number of potential entry points present themselves. First, Balkania is moving towards accession to the European Union, although there is as yet no firm timetable for this. The country must meet a raft of detailed conditions and is subject to scrutiny on all of them. EU accession would complement a range of other multilateral commitments and memberships, such as NATO and the Council of Europe, that set standards of governance. The incentives for EU accession are substantial and therefore create a host of leverage points and bargaining chips that USAID can use to introduce anti-corruption programming. Other entry points result from severe fiscal constraints, economic and political pressure to restructure and to reduce unemployment, and the country's need for assistance in addressing severe environmental degradation.

Trade-offs are likely to be numerous. For example, efforts to improve social safety nets and to inject credit into enterprise development run the risk of stimulating corruption, at least in the near term. This risk arises from remaining weaknesses in public sector financial control systems and in the management and oversight of the state development banks and cooperatives through which increased credit will be directed. Policymakers will need to decide if the risk is worth taking. Can corruption and the resulting distortions be kept sufficiently within bounds to meet the objectives of these programs, so as to stem the erosion of living standards and stimulate the growth of competitive small and medium-sized enterprises? If so, the trade-off might well be acceptable, and indeed the program may play an important role in establishing a social balance that can maintain a low-corruption equilibrium.

With regard to USAID's anti-corruption themes, summarized in the formula "TAPEE," Balkania provides a context where all of its elements could be pursued. Relative to other countries in the E&E region, Transparency and Education have made some headway (albeit limited), and thus USAID might opt to emphasize the other elements where weaknesses are even greater: Accountability, Prevention, Enforcement.

Strategic targets. In Balkania, direct anti-corruption interventions and complementary reforms are much more likely to bear fruit than in the other country scenarios. Historical legacies, the quality of transition to a liberal political and economic order, and the continued erosion of control and autonomy by old elites have ushered in a comparatively open and developmental political regime, along with increasing separation of state and market operations. Thus, it will probably be reasonable to take steps to strengthen the courts, administrative law, audit, public sector and white collar crime enforcement, legislative oversight, transparency and freedom of information, participatory budgeting, and the like. Many, if not all, of these are suggested in USAID's TAPEE framework. Some of these steps involve long-term reform and capacity development. Especially in these instances, the strategic planning process will need to secure the international community's consensus on these goals, with a view to mutually supportive and consistent programming.

TABLE 6: ANTI-CORRUPTION STRATEGIC FRAMEWORK COMPARISONS

Scenario	World Bank (2000) Description	Strategy		
		World Bank (2000)	USAID (2002)	Additional Elements
“Balkania”	Medium State Capture/ Medium Administrative Corruption	Promote further reforms in civil service, public finance, procurement, and judiciary	Accountability, Prevention, Enforcement	Emphasize employment growth, electoral reform, trade and financial sector integrity, effective responses to white-collar and organized crime
		Introduce greater transparency into political financing	Transparency	
		Develop strong partnerships with civil society	Awareness	
“Caucasia”	Medium State Capture/ High Administrative Corruption	Build the capacity of public administration	Prevention	Support basic public order & security, economic restructuring & growth
		Develop instruments for financial management	Accountability	Improve civil servant status, conditions
		Encourage civil society	Awareness	Strengthen external watchdogs and citizen-driven accountability mechanisms
“Oligarchia”	High State Capture/ Medium Administrative Corruption	Broaden formal channels of access to the state		Strengthen corporate governance quality, campaign finance transparency
		Deconcentrate economic power through competition and entry		Build institutional checks into center-regional rivalries
		Enhance oversight through participatory strategies	Accountability, Awareness	
“Kleptokrastan”	High State Capture/ High Administrative Corruption	Deconcentrate economic power through restructuring, competition, and enhanced entry		Strengthen donor coordination, regime budget constraint, civil rights protections
		Build accountability through oversight mechanisms	Accountability	Seek opportunities to increase transparency
		Promote collective action among countervailing interests	Education	
		Stand-alone technocratic reforms will have limited impact		

DIFFERENT FORMS OF CORRUPTION: IMPLICATIONS FOR STRATEGY

USAID officials will encounter not corruption in the abstract, but rather particular forms and systems of corruption. Not only the program environment but also the donors' priorities will shape the strategic response. To illustrate what this means in context, we provide sample diagnoses of and responses to four types of corruption in "Oligarchia." We first present key features of the scenario, and then look at how to interpret and address various types of corruption. Table 7 summarizes this presentation.

Scenario Overview

Program Environment. While Oligarchia has undertaken significant reform, it has also had reform reversals and suffers from high levels of corruption. Governance capability is medium. The country is burdened with a historical legacy of authoritarianism, compounded by a chaotic transition that rewarded elite predation and conflict over spoils.

In particular, the society suffers from severe imbalances, with the state and the political sphere providing the most opportunities. Democratic processes coexist with authoritarian tendencies, and fragmented elites competing for spoils. However, political openness is a bright spot here, with parties and NGOs proliferating and exploiting a degree of informational transparency that is highly imperfect but improving. This combination sustains high corruption but provides some hope of positive political change.

Corruption remediability in Oligarchia is weak, with poor quality in both public and private sector governance. The two sectors are related, as oligarchs—potential and actual—alternate between official and private sector roles, cutting self-interested deals, suborning or intimidating potential opponents, and inflicting major harm on the economy. Corruption is comparatively high, entrenched, and systematic—but not centrally disciplined in such a way as to limit the damage. The bright spots here are the dynamism of the civic and private sector, the contestability of offices, and the relatively high awareness of corruption as a factor in recent crises. Dynamic trends are unpredictable: economic growth and political change, episodes of reform, and a struggle against oligarchic control and governance failure that might succeed or fail.

Leverage is also low here. Location or strategic (e.g., defense) assets give it high strategic value, while its relatively large economy and population mean that aid funds (and other "soft" revenues) do not jeopardize its overall fiscal constraint. There is no real prospect of EU accession (at least in the medium term), and trade and investment are proportionately low as a result of weak governance and economic policy. Developmental constraints include a deep legacy of authoritarianism, counterbalanced by dynamic civic and small-medium enterprise sectors. In this case, tangible international leverage for reform exists only episodically, and is usually weak.

In Oligarchia, USAID's posture is at its weakest. All values are low. Donor coordination suffers not from the strength of the EU—since accession is not on the agenda—but from very low reform leverage and the ability of the government to play off donor countries against each other. Inconsistency, duplication, and competition for influence plague the donor community. USG coordination is also relatively low, for similar reasons. USAID strength is also low, in part because available resources—which have been cut in response to Congressional inquiries—are inadequate to the task of influencing anti-corruption efforts in the country.

Strategic Considerations. Vulnerabilities are many. The emergence of regional state-business fiefdoms, oligarch-backed industrial conglomerates (including banking and media companies), and struggles over natural resource rents and other spoils all send worrisome signals about corruption trends in the future. Alternatively, increasing economic competition, political

openness, and civic activism (bringing in the growing strength of the commercial class) might turn this tide and bring about a low-corruption equilibrium over the long term.

The clearest entry points in this scenario arise from the central government's desire to defend and augment its authority by (a) gaining the upper hand in its struggles with regional and sectoral powers, and (b) improving its status and building more productive linkages with the Western industrial democracies. This interest suggests several key areas of initiative. These would include meeting international governance and investment standards, reforming the fiscal system, restructuring weak sectors of the economy, and improving the framework of intergovernmental relations. These are natural arenas for anti-corruption programming.

Several trade-offs will need to be faced. Cooperation and capacity-building in government may in the near term strengthen corrupt anti-reformist networks and have the result of suppressing emerging autonomous centers of power. The long-term impact may be further to entrench corruption and delay reform. Further privatization and decentralization may intensify the growth of petty fiefdoms and uncoordinated corruption, thereby enabling corruption to spin out of control. On the other hand, increasing economic and political competition, especially if it encourages the growth of the middle class, provides some hope of a long-term process of bringing corruption under control—even if this stimulates corruption in the near term.

In terms of TAPEE, the situation in Oligarchia appears to offer insufficient support for effective prevention and enforcement activities. This are subject to being undermined or even abused. USAID can more productively focus on transparency, accountability, and education activities in order build norms and structures of restraint from the bottom-up and outside-in, emphasizing non-governmental initiatives.

Strategic targets. Frontal assaults on corruption, for the most part, are not very likely to succeed. Too many elements of government, the economy, and society are seriously compromised. Government-centered approaches in particular risk strengthening anti-reform elites and inviting further abuse. NGO and some private sector-based approaches, and perhaps some regional initiatives as well, have some hope of succeeding, since these sectors are less compromised and much more friendly to idealism and reformism.

Illustrative Forms of Corruption: Diagnosis and Response

Corporate-bank collusion in Oligarchia serves as a mechanism for self-enrichment and self-perpetuation of a narrow elite dominated by robber barons or “oligarchs.” Responses to this problem should perhaps focus less on state regulatory capacity and more on such structural approaches as tightening the overall regime budget constraint, increasing private sector competition, encouraging foreign participation in the banking sector, and campaign finance reform. This would serve to help right the balance among social and political elements, thereby advancing the day when oligarchic corruption systems can be attacked head-on.

Diversion of state oil revenues further strengthens the elite and softens the budget constraint, fueling systems of corrupt exchange. The autonomy of elites from popular fiscal control is both cause and objective of this type of corruption, which relies on manipulation of the privatization and regulation processes, with the assistance of media controlled by the same oligarch-dominated corporate groups. In this situation, USAID would do well to press hard for donor-country coordination to harden the regime's budget constraint and to press for greater financial transparency in the public and private sector. Corporate governance in general requires attention, and this includes media company control. Also, USAID can usefully press for sustained long-term attention to building basic institutions of the rule of law and oversight.

Bribery in business regulation not only dampens SME growth but distorts enterprise growth in favor of connected companies, while it sustains patronage and protection networks. This form of corruption is linked to the spoils system prevalent in national and local government, and also reflects the priority interest of the regime in mineral extraction industries rather than an entrepreneurial economy. In response, USAID will need to emphasize electoral reform and intergovernmental restraints on commercial regulation, and on stimulating enterprise growth and expanded tax revenues to change the incentives driving the sale and abuse of office.

With respect to *corruption in the customs administration*, this not only suppresses trade but delays reform and strengthens patronage networks that use it as a source of campaign funding. USAID may want to support the growth of competitive export-oriented SMEs that will likely support effective customs administration in the future. The restructuring of customs, as well as campaign finance reform, might better be addressed at a later point, when the political balance and economic imperatives are more supportive.

TABLE 7. OLIGARCHIA CORRUPTION CONCERNS AND RESPONSES			
Form of Corruption	Importance	Causal Diagnosis (individualist/ structural)	Anti-Corruption Strategy Components
Corporate-bank collusion to engage in fraud & self-dealing	Significant distortion of credit allocation, bank oversight, corporate governance increase risk of financial crisis & enable oligarchy to perpetuate domination	Oligarchic self-interest leads to continued intermingling of elite, state, company, bank interests; regulators kept subordinate to political interests; elite deeply involved in self-enrichment & capital flight; public/private sector office serves not as opportunity for competition but as mechanism of control & enrichment	Seek donor country coordination to tighten overall budget constraint; support FDI, increased competition, campaign finance transparency, corporate & bank restructuring & governance reform
Diversion of state oil revenues to personal and campaign accounts	Strengthens elite & regime fiscal autonomy from population, fuels corruption networks & perpetuates their dominance	Nomenklatura/oligarch manipulation of state ownership & privatization to maximize control of oil sector; political control of oil sector audit/oversight; elite insulation from citizen electoral/fiscal control and from criticism by captive media	Seek donor accord on country budget constraint & budget transparency; provide long-term support to improve judicial & audit systems, independent watchdogs, corporate governance & money-laundering reforms, competitive markets, (esp. in energy), electoral reform; support transparency of ownership & professional standards in media
Bribery in business licensing & inspection	Barrier to SME entry & growth, a major source of economic dynamism; increases role of facilitators & mafia; sustains local patronage systems	Predominant interests of resource extraction and large corporate network interests mean little interest in favorable SME environment; spoils system means sale of regulatory offices at prices reflecting bribery income; admin & legislative oversight need to be kept weak and/or share in benefits	Support electoral reform, restructuring of inter-govt. relations & disciplines, competitive market-oriented federalism, deregulation, economic growth with increased private sector opportunities & tax revenues to pay official wage bill
Bribery, fraud & collusion in customs administration	Illicit/uncertain tax on trade, encourages smuggling, delays further trade reform	Customs is a patronage base and source of campaign finance; reform of schedules and procedures delayed	Strengthen support & enabling environment for trade-oriented SMEs, campaign finance reform, customs admin. restructuring

ADJUSTING USAID PORTFOLIOS IN LIGHT OF STRATEGY

In developing and implementing anti-corruption strategies, USAID missions are not writing on a blank slate. They already have detailed programs. Where strategy will have an impact is in designing new programs and activities, as well as in adjusting current portfolios to reflect anti-corruption priorities. In this section, we illustrate how the strategic framework presented above can provide guidance in this process. For illustrative purposes, we draw on the “Kleptokrastan” scenario.

Scenario Overview

Program Environment. Kleptokrastan is resource-rich and authoritarian. All governance capability variable values are low here, suggesting ineffective, predatory governance and very little capability to constrain corruption. Adverse legacies of totalitarianism and clan divisions exert a harmful influence. In dynamic perspective, hopeful signs include trends in the direction of autonomous social and political power centers—still suppressed to a great extent by a controlling regime—and some spread of economic growth benefits, creating a medium to long-term prospect of greater balance in economic and political opportunities. The modest size of the population, the general level of education, and the absence of extreme poverty support this hope.

In Kleptokrastan, corruption remediability is weak. High values for the extent and entrenchment of corruption accompany low values for public and private sector governance quality. Corruption is rampant and somewhat unpredictable, with opportunism and network or clan-based division of spoils coexisting. The potentially positive feature here is a comparatively autonomous elite operating within an authoritarian regime characterized by some professionalism—hence the hope, eventually, of bringing some discipline to the organization of corruption. In the private sector, growth is fueled by mineral revenues, with some enterprise competition and commercial classes slowly emerging. However, the quality of corporate governance is quite low, due to the complete intermingling of business and policy interests and the flow of natural resource and illicit trafficking revenue into the pockets of the elite.

Reform leverage is low in Kleptokrastan. The country has significant mineral extraction rents and strategic importance based on location and other strategic assets. At the same time, one would expect this country not to be strongly integrated into the international economy (apart from FDI in the mineral sector) or within regional arrangements. In this case, the international community as a whole has comparatively little leverage, in part because this country is in a position to press its interests and to play solicitous foreigners off one another.

Here, USAID is in a posture of intermediate strength. Donor coordination is low, although the U.S. takes the lead in dealing with the host country along with other major parties at interest, such as the World Bank, Asian Development Bank, Russia, and the investor community. Within the U.S. Government, there are differences over priorities to be assigned to facilitating mineral sector investments, dealing with a range of governance and security concerns, and dividing labor among agencies. Overshadowing all this are the strategic issues reviewed previously. On the other hand, USAID’s capabilities for engaging in anti-corruption work in the country are relatively high, since its funding has recently been augmented, it has effectively given top priority to corruption issues, and the expectations of Congress and the State Department with respect to near-term improvement in the country are quite low. This alone does not translate into an ideal aid environment, but does suggest relative USAID strength here as compared to the previous scenario. This, of course, does not change the fact that virtually all other factors in the program environment within this country are negative.

Strategic Considerations. Vulnerabilities come in many forms. Economic dependency on mineral rents, along with other strategic advantages, nurtures an ex-nomenklatura elite that is both free of citizen voice in fiscal control and predatory in practice. The threat that political change seems to pose to the elite, along with the potential volatility of clan differences and turbulence in Central Asia generally, encourages the regime's policies of media control, restrictions on civil rights, and continued subordination of agencies of restraint. Governance thus becomes not only worse but increasingly irremediable.

Many of the same features may also provide entry points. Kleptokrastan's economy depends substantially on mineral (i.e. petroleum sector) rents, and foreign direct investment is critical to the development and marketing of those resources. However, this cuts both ways. Current U.S. dependency on foreign sources of oil, third-country investor competition for concessions in Kleptokrastan, and the influence of the petroleum lobby on U.S. foreign policy, all tend to reduce the leverage that USAID might have here. American investment is undeniably of some importance to the country, and USAID should focus on building anti-corruption elements into programs relating to foreign investment and natural resource management.

As in Oligarchia, there will be difficult trade-offs. Strengthening official agencies of restraint risks strengthening elites that largely control the state, thereby inviting further abuse. In this case, furthermore, the international community as a whole seems to be making matters worse, loosening the budget constraint and compromising governance interests in the pursuit of advantage in the strategic and mineral investment arenas.

TAPEE elements will be especially important, given the fact that USAID is unlikely in current circumstances to push the government successfully into fundamental reform. Transparency should receive highest priority across USAID's portfolio, although the areas in which this can be safely pursued are limited. Education should also be emphasized, with a view toward building habits, norms, and eventually institutions that embody anti-corruption values. Practices of accountability might also be built into programs in ways that do not impose undue risks on participants.

Strategic targets. As in Oligarchia, frontal assaults are not likely to be effective and indeed may intensify abuse. Upstream approaches that increase external accountability, such as administrative procedure and appeals systems, would also be subject to manipulation and control, and may place complainants at risk.

Adjusting Aid Portfolios

In Table 8, we provide a matrix showing the extent to which the main donor programs aim at the "Strategic Targets" discussed in the Kleptokrastan scenario above. This material, in simplified form, represents a summary of donor programs in an actual Central Asian country. A major weakness here is our inability to capture and incorporate complete information on sub-programs, individual initiatives, and implementation practices on the ground – all of which could be important for our purposes.

Nevertheless, the information we do have strongly suggests that, while most of the strategic targets are being addressed, there are also some gaps that could well be addressed by more meaningful coordination among donors (which the matrix suggests is insufficient). One area where this appears to be needed is in tightening the regime's budget constraint. USAID intends to cut back aid to the central government when oil revenues make this unnecessary. However, the donors as a group have provided billions of dollars in loans and grants, and significant corruption in the government has apparently not significantly reduced the flow of funds. Also, an area where

large investments may not yet be justified, and where leverage might be used more in preference to the supply of funding and technical assistance, is the development of oversight mechanisms. Certainly where these form part of the central government structure, there is little reason currently to expect such institutions to have real political autonomy. Indeed, if their powers are not carefully delimited, they could become instruments of abuse.

Dynamic effects must be considered. Of critical importance here is an understanding of the near-term and long-term anti-corruption effects of the range of U.S. (and other) aid interventions—whether undertaken with an anti-corruption rationale or not. One obvious complication is the possibility that reforms associated with governance improvements might be designed or sequenced in ways that increase corruption. For example, separate programs might be launched in the areas of financial sector liberalization and banking supervision. Liberalization could easily move ahead in advance of the regulatory and supervisory program, and as a result introduce chaotic and corruption-inducing conditions. This points out the importance of careful definition of, and consensus on, the appropriate programmatic and time perspectives. A restricted menu of anti-corruption program options focused on directly attacking corruption symptoms will likely lose sight of the equally important (in many cases more important) corruption issues embedded in economic restructuring and reform efforts. Even with a broader programmatic perspective, excessive focus on near-term (anti) corruption effects will obscure the important long-term (anti) corruption outcomes that may permanently reverse the short-term effects.

TABLE 8: STRATEGIC TARGETS AND DONOR PROGRAMS IN KLEPTOKRASTAN¹⁶

Strategic Targets/Donors	USAID	World Bank	Other Donors
Deconcentrate economic power	SME support, finance & enabling environment projects Energy industry & competition regulation	Finance & enterprise development loan Real estate registration pilot	GTZ devel. cooperative mgmt TA, regional economic promotion pilots ADB farm enterprise loan, urban small business development EBRD small business projects
Build accountability through oversight mechanisms	Fiscal reform: audit Political process: legislative oversight Local governance Health care management	Legal reform loan Treasury modernization loan	GTZ legal reform promotion UNDP ombudsman support, public admin program
Collective action among countervailing interests	Support for civic organization development Public awareness re energy pricing & services, health care		UNDP participatory social devel., civil society & social ptrnships projects
Strengthen donor coordination	Active coordination with other donors		UNDP co-finance arrangements
Tighten regime budget constraint	U.S. asst. \$1.7 bill. since '92, \$650 via USAID, \$45 mill. USAID '02 program. Aid to central govt. will decline as oil revenues rise.	2002: \$1.8 bill. loans outstanding, of which \$1.1 bill. adjustmt loans. Total \$1.3 bill. disbursed.	
Strengthen civil rights protections	Political process: legislature Media & info: civic education		GTZ legal reform promotion UNDP legislative & human rights program
Increase transparency	Fiscal reform: budget transparency Media & info: journalism		UNDP public admin. & civil service program

¹⁶ Based on current donor programming in Kazakhstan. USAID Regional Mission for Central Asia (2000), "USAID's Assistance Strategy for Central Asia 2001-2005," mimeo. USAID Central Asia Region (2002) "Kazakhstan Portfolio Overview," mimeo. Web-based documentation from the World Bank (www.worldbank.org.kz), UNDP, GTZ, EBRD (www.ebrd.com/projects/psd/country/kazak.htm), ADB.

CONCLUSION

The general analytic framework provided here should be seen as a starting point in developing a detailed strategy and program matrix that faithfully represents the situation at hand. Its chief value lies in illustrating the interaction of corruption with a range of aid program objectives and the importance of inclusive long-range planning.

The benefits of strategic planning increase as more of the international stakeholders – other US government agencies, other donor governments and agencies, private sector actors and NGOs – are brought into the process of strategy formation. Only such an inclusive process can incorporate the strategic approach into programs across the board, in each sector and by each external actor, to counter the tendency of corruption to find alternative vehicles and paths. This strategic framework is designed to foster a rich discussion and planning process among these stakeholders. The resulting plans and programs should be better positioned to help bring corruption under sustained control.

STRATEGY-RELEVANT VARIABLES IN THE PROGRAM ENVIRONMENT

GOVERNANCE CAPABILITY

This cluster of variables (arrayed in Box 1) reflects a society's key capabilities for effective governance, including the socio-economic characteristics of elites and society generally, and the openness of the political regime. The lower the overall value of these governance variables, the less likely it is (*ceteris paribus*) that aid interventions will engender reform, that reforms will in any case take place, that such reforms as are adopted will be implemented and sustained, and that governance will actually improve significantly in the near to medium term.

The first sub-group within this cluster deals with the nature of the governing regime. Basic stability and public order are foundational—without this, it makes little sense to proceed with technical governance reforms. Next in importance is the cohesion of the elite, along with its tendencies to be either “developmental” or predatory. An elite would be considered developmental if its governance style is consistent with a long time-horizon, broad-based economic growth, and long-term development—regardless of absolute levels of corruption or the existence of a democratic political order. Cohesion is important for its relationship to stability, policy consistency, and the level of discipline in the organization of political exchange and corruption. High values of all these variables correlate with high regime cohesion, which in turn relates directly to a country's ability to restrain corruption.

The next sub-group of variables deals with broader issues of social structure and capability. These include mobility and sustainable balance (Johnston 1997), along with historical legacies and public attitudes to governance and corruption issues. These factors also directly correlate with a society's ability to constrain and to address corruption. They exert this influence by supporting mobility and open political exchange—thus generally limiting incentives for corruption—and by enabling effective political checks and balances, which can both limit corruption and make it easier to address.

A third sub-group concerns pluralism, openness, and contestability in the political order. These variables include the extent to which the political order is democratic (as opposed to authoritarian) in practice, recognition of civil and political rights, and the quality and availability of governance-related information. These are the essence of liberal democratic governance. A fourth sub-group brings in broader social concerns, i.e., whether power is indeed dispersed among political and social centers of influence such as traditional ethnic or religious formations, political and social movements, and economic sectors. These factors strongly influence governance quality and the likelihood that significant corruption can be overcome—absent a developmental authoritarian regime.

As with all the variables discussed in this paper, interrelationships are critically important. In this context, the quality and cohesion of elites is especially necessary in an authoritarian political order. Governance structures, particularly agencies of restraint (see the next part), are especially important in the absence of a developmentally-oriented elite. Thus, for example, an authoritarian

order with a high-quality elite will usually have more effective administration and less corruption than a democratic order with weak or compromised agencies of restraint.

BOX 1: GOVERNANCE CAPABILITY VARIABLES

Governing regime quality:

- Stability and public order
- Cohesion of ruling elites
- Developmental (vs. predatory) quality of elites

Social and political balance:

- Favorable historical patterns, legacies (e.g. social capital, ethnicity/status, networks, governance norms)
- Sustainable balance of economic (private sector) and political (public sector) opportunities across society
- Openness/accessibility of elite positions
- Quality of elite and public attitudes vis-à-vis governance and corruption

Political openness:

- Factual importance of democratic, as compared to authoritarian, governance mechanisms
- Extent of civic and political space: free expression/media, civil rights, contestability
- Level of transparency, quality of information flows
- Pluralism, dispersion of power among autonomous centers

CORRUPTION REMEDIABILITY

This cluster of variables concerns the quality of governance structures in the public and private sectors, along with the intensity and remediability of corruption problems; these variables are summarized in Box 2. The first sub-group of factors deals with government institutional quality. The focus here is on checks and balances, professionalism in officialdom, and the quality of the government's anti-corruption effort. These factors can to some degree compensate for deficits in governance capability measures, but they relate in different ways to those previous variables. For example, a high-quality officialdom can play an important role in either a developmental authoritarian order, or in a democratic order with effectively independent agencies of restraint—but it is unlikely to do so absent these circumstances. The last factor, the government's anti-corruption effort, can address localized weakness but cannot make up for low values in most of the preceding variables. Its beneficial effect depends on generally effective governance.

The second sub-group of variables focuses on the private sector. These are important in two ways, determining both the likelihood of corrupt behavior within the private sector and the probability that blurred corporate boundaries will encourage overlap and mutual distortion between public policy and enterprise management. The first three listed factors deal directly with

these concerns. The degree of enterprise autonomy from political control, along with the quality of corporate governance, determines whether a company is run for the benefit of all shareholders or that of insiders and political cronies. Higher values here denote stronger governance quality and capability. The importance of state linkages has the opposite effect, thus showing the direct relationship of state (or politician) control rights in transition settings to corruption. In all of these first three instances, adverse private sector governance reduces a society's ability to remedy corruption once it has become a significant problem. The last variable in the list has an "upstream" effect. Competition and dynamism in the enterprise sector, on the one hand, and the advancement of private interests through state and political influence on the other hand, do not easily co-exist. Most clearly, the latter dynamic reduces market-based governance, while well-governed and competitive markets tend to constrain and clarify the economic role of the state – and to keep corruption in check.

The last sub-group of variables in this cluster deals directly with corruption. The first two factors in the list reflect its scope and level of systematization. To the extent that corruption significantly affects all or most components of government, and to the extent it is an established system (as opposed to being merely localized and opportunistic), a society will have greater difficulty making inroads against it. On the other side of the coin, a more disciplined system of corruption is likely to keep the overall level of extraction and negative externalities within bounds. Decentralized, discretionary, and especially chaotic corruption is thought to be the most lethal, at least in economic terms (Shleifer and Vishny 1998). The remaining three variables are based on the World Bank (2000) taxonomy of state capture and administrative corruption. In our view, particularly important aspects of these phenomena are: the extent to which state capture compromises whole branches or sectors of public authority, the linkage of administrative corruption to systemic networks, and the extent and manner in which agencies of restraint are compromised. The stronger such tendencies are, the less likely any effective response to corruption will materialize.

BOX 2: CORRUPTION REMEDIABILITY VARIABLES

Integrity of governing institutions:

- Level of (de facto) autonomy in agencies of restraint: legislature, public service, courts & law enforcement, audit & control systems, central bank, regulatory agencies, local governments
- Level of professionalism, meritocracy, and remuneration for public officials
- Quality of anti-corruption policy, strategy, institutions, outputs

Quality of private sector governance:

- Extent of (de facto) enterprise autonomy & private ownership
- Quality of corporate governance, including transparency of ownership structures
- Importance of state linkages (ownership, lobbying, control/intervention, contracting) to enterprise performance
- Ease of entry, quality of competition, dynamism

Scope and entrenchment of corruption:

- How widespread across parts of government, political forces/parties, elites, regions?
- How entrenched/systematized vs. episodic/opportunistic?
- Industrial organization: how disciplined vs. chaotic?
- Extent of state capture
- Extent of administrative corruption (and linkage to patronage networks)
- Agencies of restraint: extent of state capture & admin. Corruption

REFORM LEVERAGE

This group of variables (presented in Box 3) relates to a governing regime's incentives to reform and to rein in corruption. These factors influence the overall likelihood of reform, along with the leverage available to domestic reformers, international organizations, and donor countries. The higher the value of reform leverage, the greater the impact we can expect from an aid program investment (*ceteris paribus*).

The first sub-group of variables, entitled "Strategic Value," recognizes the importance of a country's size, geopolitical role, economic importance, and strategic assets in determining reform incentives—and in particular, a regime's susceptibility to international pressure for reform. The higher a country's strategic value is, the more geopolitical interest and donor support it is likely to attract—but this interest may or may not encourage governance improvements. To the contrary, strategic value is more likely to serve as leverage for the country, or its ruling elite, to extract rents in diplomatic and donor negotiations. The first three variables in this group bear an inverse relationship to reform leverage—i.e., the larger their values for the country in question, the less leverage there is for actors such as USAID. The variable dealing with trafficking and borders is

similar, in that a high value indicates strategic importance, which in turn attracts international interest. At the same time, this factor potentially has a zero-sum relationship with reform leverage: the more a ruling elite can extract from illicit commerce across porous borders, the more it has to lose from reform and the more likely it is to resist.

High strategic value countries present a problem for USAID. Near-term diplomatic gains will likely hold the greatest interest for all donor countries, and as a result, alignments to engage in coordinated action in favor of reform become less likely. International tolerance of weak governance and high corruption is the price of near-term strategic gain. If, on the other hand, USAID can make common cause with those international interests holding leverage over strategic assets in the country—e.g., investors with controlling interests or dominant market positions—then USAID can thereby gain reform leverage.

In the case of the second sub-group of factors, “International Integration,” the relationship to reform leverage is direct: the more integrated a country is, the greater its incentives to reform and susceptibility to external pressure are likely to be. This has been most obvious where countries have a realistic prospect of eventual accession to the EU. Whether general leverage translates into an ability by USAID to push for reforms with an anti-corruption impact depends on USAID’s posture (see below), including its relationship to arrangements such as the EU and the likelihood of coordinated external action.

The third sub-group of variables, “Firmness of Budget Constraint,” in general also correlates directly with reform leverage. Most clearly, a stringent fiscal bind, along with the absence of natural resource revenues and other “soft” revenues as major financial sources, would tend to increase reform leverage. As suggested above, illicit revenue sources can be reduced by means of reform, but this is precisely what makes their beneficiaries resist reform—some conflicting incentive is needed if reform is to take place. The aid flow variable has two conflicting impacts. For any predominant donor, or for donors as a group (assuming they can act collectively), a high value here means high leverage. By contrast, for an individual (non-dominant) donor, and for domestic reformers who cannot influence the flow of aid, high aid flows suggest low reform leverage, having an impact much like mineral revenues.

The last sub-group, “Developmental Constraints,” includes variables reflecting situations that may not influence incentives for reform, but that pose severe obstacles to a country’s ability to engage in reform. For this reason, these factors are also associated with weak governance and high corruption. These factors include political instability, limitations on authority, fractionalization, and adverse legacies.

BOX 3: REFORM LEVERAGE VARIABLES

Strategic Value:

- Political and economic importance: size, fixed investments, market & political links
- Strategic location/facilities: ports, pipelines, bases, staging grounds near front
- Weapons and defense industries/facilities: WMD, aerospace, scientists
- Role in illicit trafficking networks, difficulty of controlling borders

International Integration:

- EU accession prospects/schedule
- NATO membership/entry
- Other regional & international disciplines: WTO, OECD, Council of Europe, SPAI
- Role of international trade & foreign investment in the economy

Budget Stringency:

- International fiscal constraints: debt burden, capital movements, balance of payments
- Oil or mineral wealth as proportion of revenue sources
- Aid flows as proportion of public sector budget
- Other ‘soft’ fiscal resources: weapons/drug trafficking, off-budget enterprises, corporate asset control, state bank directed credit

Developmental Constraints:

- Post-conflict situation
- Severe economic shock, transition crisis, disaster
- Non-autonomous status
- Inherited ethno-religious rifts, class hierarchies, cultural disabilities
- Political crisis and flux

USAID INFLUENCE

This set of factors (presented in Box 4) concerns the posture of USAID in a given country, i.e., its relationship to other donor programs, its influence on the coordination of overall U.S. policy in the country, and the extent to which its existing programming trends are supportive of anti-corruption objectives. The first sub-group deals with international donor coordination. Do donor countries and agencies duplicate effort and compete for influence? To what extent are their policies and strategies consistent—in general and specifically on anti-corruption objectives? These factors interact with the reform leverage variables presented above—they tend to correlate directly and exercise mutual influence. The lower the value of donor coordination, the less likely

effective anti-corruption interventions will be, and indeed the more likely it is that donors will be underwriting ineffective governance and even corruption.

The next two sub-groups concern internal U.S. Government and USAID matters. How consistent is overall U.S. foreign policy and aid with anti-corruption objectives? How much of a voice does USAID have in determining aid policies and influencing diplomacy? How powerful are other U.S. Government agencies and outside grantees and contractors in influencing USAID strategies and program implementation? Within USAID, is there effective agreement and coordination, especially on anti-corruption goals? Are the resources and time allocated to this area adequate, and what in fact are the opportunities to deploy these effectively—e.g., political openings, USAID influence with key power brokers, effective partnerships with credible reformers? High values on all these variables translate into greater likelihood that effective anti-corruption interventions will be possible.

BOX 4: USAID INFLUENCE VARIABLES

Donor coordination:

- Extent of program overlap among donors
- Competition to monopolize activities/ministries
- Consistency across donors re conditionality, policy dialogue
- Shared anti-corruption objectives/strategies

Coherence of U.S. Government aid policy:

- Consistency of U.S. foreign policy with anti-corruption objectives
- Supportive embassy posture and relation to USAID & anti-corruption goals
- Extent of interagency cooperation (vs. competition): State, Justice, Treasury, etc
- USAID synergy with contractors, grantees, NGOs, others
- Internal USAID coordination

USAID program anti-corruption value:

- Overall resources available, existing commitments
- Importance and resources allocated to anti-corruption goals
- Available points of entry and leverage
- Appropriate time horizon and accountability

ANNEX 2

SUMMARY TABLE OF ILLUSTRATIVE CORRUPTION TYPES & ANALYSIS

Form of Corrupt Practice	Diagnosis of Causes		Responses		Cost-Benefit Issues	
	Individualist/ Narrow Focus	Structural/ Wider View	Technocratic (individualist)	Political (structural)	Status Quo	Effective Response
Corporate-bank collusion for fraud & self-dealing	Weak or politicized bank supervision; flawed corporate governance; lack of transparency & criminal enforcement	Nomenklatura-affiliated networks enriching selves and their parties or campaigns via banks, firms, state.	Strengthen & tighten bank supervision, corporate governance, transparency & criminal enforcement.	Restructure bank & firm ownership; increase FDI; tighten regime budget constraint; increase political & economic competition.	Misallocates capital, deters investment, threatens stability of financial system, feeds crony/ criminal networks, drives rent-seeking and further weakening of corporate governance. Exchange of illicit gains may enhance short-term stability and elite consensus.	Correcting this enables effective corporate & financial sectors, hence sustained & balanced economic growth; cuts crony/ criminal networks off from this source of support; discourages rent-seeking. Direct attack on corruption may backfire; restructuring takes time, political capital & sustained policy focus, and provokes opposition; short-term economic disruptions; who will take the lead?

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